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No. 03-12

IN THE

Supreme Court of the United States

NATIONAL FIRE INSURANCE COMPANY OF HARTFORD,

Petitioner,

v.

FORTUNE CONSTRUCTION COMPANY,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

BRIEF IN OPPOSITION

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QUESTION PRESENTED FOR REVIEW

Whether the decision of the Eleventh Circuit Court of Appeals presents no basis for review because it simply applied established Florida law based on the terms of Petitioner's performance bonds to the facts and circumstances of this particular case, and did so in a manner that is consistent with the decision of the Fifth Circuit as to which Petitioner asserts conflict.

STATEMENT PURSUANT TO RULE 29.6

Fortune Construction Company is a General Partnership.

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STATEMENT OF THE CASE

A. Reply to Petitioner's Statement of the Case

Petitioner's brief contains misstatements of fact and law, identified below, in accordance with Rule 15(2).[1] Respondent also notes that Petitioner's Appendix contains only the decisions and orders of the district court and of the Eleventh Circuit, and Respondent therefore relies upon the Petitioner's Appendix as containing the only materials upon which Petitioner relies as essential to the Court's understanding of the Petition. Rule 14(1)(i)(v). Petitioner's brief, however, contains almost no Appendix references to support its factual recitations, and many of its factual recitations are not supported by anything in the Petitioner's Appendix.

Neither has Petitioner included any recital of the terms of the surety bonds and construction contracts upon which its question presented for review by this Court is based. Respondent respectfully submits that these deficiencies in the Petition – which also hinder Respondent's ability to respond – are sufficient basis for the denial of the Petition without more. Rule 14(4).

Respondent also believes, however, that the facts material to the determination of whether this case presents any basis for exercise of this Court's jurisdiction are few and undisputed. All such facts appear on the face of the Eleventh Circuit's decision, which is included in the Petitioner's Appendix, at pages 1 through 38. Respondent accordingly presents a brief statement of the case with

1. Respondent makes reference to the Rules of the Supreme Court of the United States herein as "Rule __."

Appendix references to the undisputed material facts as recited in the Eleventh Circuit's decision.

B. Respondent's Statement of the Case

1. The undisputed material facts

The question presented in the Petition arises out of the Eleventh Circuit's decision as to the duties and obligations owed by Petitioner National Fire Insurance Company pursuant to certain performance and payment bonds issued by Petitioner in connection with two apartment complex construction projects in South Florida, known as the Winston Park and West Brickell projects. (Petitioner's Appendix, p. 2).[2] Respondent Fortune Construction Company was the general contractor on the projects and Arkin Construction Company was its subcontractor. (Petitioner's Appendix, p. 2). Arkin obtained the National Fire surety bonds to secure Arkin's payment and performance obligations under its subcontracts for the projects. (Petitioner's Appendix, p. 2).

The Winston Park project payment and performance bonds were selected by National Fire from standard industry forms, while the West Brickell project payment and performance bonds were separately drafted by National Fire. (Petitioner's Appendix, p. 2). Each of the performance bonds and each of the payment bonds, however, specifically "incorporated the appropriate subcontract between Fortune and Arkin by reference." (Petitioner's Appendix, p. 2).

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2. References to the Petitioner's Appendix appear as (Petitioner's Appendix, p. __). Respondent has also provided an Appendix with this brief, which is referenced as (Respondent's Appendix, p. __).

The ***pivotal fact*** for purposes of this Court's determination of the question presented for review is undisputed, and was stated in the Eleventh Circuit's decision as follows: "The construction subcontracts [between Fortune and Arkin] each contained a clause obligating Arkin to pay liquidated damages for delays in completing the projects." (Petitioner's Appendix, p. 3). Specifically, as the Eleventh Circuit also noted: "The Winston Park Subcontract provided for liquidated damages of $35 per day per incomplete apartment and $1,000 per day for incomplete common areas. The West Brickell Subcontract provided for liquidated damages after a specified date of $30 per day per incomplete apartment." (Petitioner's Appendix, p. 3).

Arkin began experiencing financial difficulties while working on the two projects, and failed to meet various payment obligations to subcontractors and suppliers. (Petitioner's Appendix, p. 2). Delays ensued, and Arkin eventually abandoned the project altogether. (Petitioner's Appendix, pp. 2-3). Fortune initially tried to work through the problems with Arkin, but declared Arkin in default when Arkin abandoned the projects. (Petitioner's Appendix, pp. 2-3). Fortune notified National Fire of Arkin's default, and demanded that National Fire perform its obligations under the performance bonds for completion of Arkin's work on the projects. (Petitioner's Appendix, p. 3). National Fire did not complete either project despite demand, and Fortune was compelled to perform the subcontracts. (Petitioner's Appendix, p. 3).

2. The litigation over the obligations and entitlements created by the subcontractor's defaults

Litigation thereafter ensued between National Fire, Fortune, and Arkin over a variety of issues, including National Fire's asserted subrogation rights for having paid some of the subcontractors and suppliers under the payment bonds, Fortune's asserted rights to damages from Arkin for breach of the construction subcontracts, Fortune's asserted rights to recover for National Fire's breach of the performance bond, and the priorities amongst the parties' rights to funds held by Fortune consisting of the amount left from the contract price after completion of the projects. (Petitioner's Appendix, pp. 3-5). The litigation was initiated by National Fire in the federal district court for the Southern District of Florida on the basis of that court's diversity jurisdiction. (Petition, p. 3).

The only issue here is Fortune's claim for the liquidated delay damage amount that was owed to Fortune under the terms of its subcontract with Arkin. (See Petition, p. i, "Questions Presented for Review"). Fortune contended that because National Fire's performance bonds specifically incorporated the terms of the Arkin subcontracts by reference, and since the Arkin subcontract contained a specific clause obligating Arkin to pay liquidated damages for delays in completing the projects, Fortune was entitled to recover the liquidated delay damage amount from National Fire. (Petitioner's Appendix, p. 20). National Fire's position was presented in a complex manner – via seven different motions for partial summary judgment – making various arguments over the priorities of rights and obligations amongst the three

parties. (Petitioner's Appendix, p. 5).[3] The argument made by National Fire that is pertinent here was that despite the fact that its performance bonds incorporated the Arkin subcontracts by reference, it should not have to pay the liquidated delay damage amounts owed under the Arkin subcontracts because the bonds did not say *on their face* that they would cover delay damage amounts. (Petitioner's Appendix, p. 21).

3. The Eleventh Circuit's decision

The Eleventh Circuit correctly noted that it would be bound to follow Florida law in deciding the issue in this diversity case, and therefore "look[ed] to Florida law to see what a surety's obligations are in the circumstances of this case." (Petitioner's Appendix, p. 21). The Eleventh Circuit then determined that it should follow the Florida Supreme Court's decision in *American Home Assurance Co. v. Larkin General Hospital, Ltd.*, 593 So. 2d 195 (Fla. 1992). The *Larkin* Court had decided, based on the unremarkable proposition that "[a] bond is a contract, and therefore, is subject to the general law of contracts", 593 So. 2d at 197, that "[t]he language in the performance bond, construed together with the purpose of the bond" determines the liability of the surety under the bond. *Id.* at 198. (Petitioner's Appendix, p. 22). The bond in *Larkin* did not include any language that specifically provided for payment of delay damages, and the *Larkin* Court held that *for that reason* the surety would not be liable for delay damages. (Petitioner's Appendix, pp. 21-22).

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3. As the Eleventh Circuit pointed out: "National Fire's attempt to break this case into little pieces seems to have contributed to the confusion below." (Petitioner's Appendix, p. 31).

The Eleventh Circuit noted the critical factual distinction between the *Larkin* facts and those presented here: ***"Importantly for purposes of our analysis, there was no liquidated or other type of damages provision in the underlying contract."*** (Petitioner's Appendix, p. 21) (emphasis added). The Eleventh Circuit then went on to apply the principle enunciated in *Larkin,* i.e., that a surety will not be liable for delay damages unless its bond contract language specifically provides coverage for delay damages, to the facts and circumstances presented in the instant case with the following discussion:

The *Larkin General Hospital* court noted:

> [t]he purpose of a performance bond is to guarantee the completion of the contract upon default by the contractor. Ordinarily a performance bond only ensures the completion of the contract. The surety agrees to complete the construction or to pay the obligee the reasonable costs of completion if the contractor defaults.

Id. at 198 (citations omitted). Although a surety's liability is coextensive with that of the principal, "the surety's liability for damages is limited by the terms of the bond." *Id.* Therefore, the Supreme Court of Florida found that "[t]he language in the performance bond, construed together with the purpose of the bond, clearly explains that the performance bond merely guaranteed the completion of the construction contract and nothing more." *Id.* (emphasis added); *see also*

> *Mycon Constr. Corp. v. Board of Regents*, 755 So.2d 154, 155 ([Fla.] 4th DCA 2000) ("Because the performance bond contains no provision for damages for delay, the surety cannot be held liable for such damages."). ***However, unlike the performance bond in Larkin General Hospital, the bonds at issue in this case expressly incorporated the subcontracts, which, in turn, do expressly provide for liquidated delay damages.***

(Petitioner's Appendix, pp. 21-22) (emphasis added). The Eleventh Circuit then went on to discuss the argument advanced by Petitioner National Fire here, i.e., that *Larkin* should be read to require the provision for payment of liquidated delay damages to appear on the face of the bond in order to be enforceable against the surety. (Petitioner's Appendix, pp. 22-23). The Eleventh Circuit rejected that interpretation because it would disregard the *Larkin* holding that the surety's obligation is to be determined from the language and *purpose* of the bond, as well as established contract principles as to incorporation by reference, which *are* applied in surety bond cases, notwithstanding Petitioner's implications to the contrary:

> *Larkin General Hospital* could possibly be interpreted to mean that a performance bond surety cannot be held liable for, or denied subrogation for, delay damages, whether liquidated or unliquidated, unless the responsibility for delay damages is specified on the face of the performance bond. However, we

do not read the decision that broadly.[4] ***The "purpose of the bond" must be considered, which requires reference to the contract secured by the bond. Where a provision for liquidated delay damages is clearly delineated in the underlying contract and incorporated by reference into the bond, the surety is on notice of the time element of performance and the contractual consequences of failure to timely perform in accordance with the contract.*** Once the liquidated damages accrue, the contractor-principal owes a debt to the obligee which is, in effect, a reduction of (or contractual off-set to) the contract price. In such event, the obligee becomes the creditor of the principal and the performance bond surety should not have superior rights to the obligee in the remaining contract balances where liquidated damages have been suffered. ***This is especially true where, as here, the surety does not remedy the principal's delay by performing the surety's obligations under the performance bond.***

While it is true that the terms of the bonds in this case do not expressly require the surety to assume responsibility for delay, "[i]t is the general rule of contract law that where a writing expressly refers to and sufficiently describes another document, the other document is to be interpreted as part of the writing." *Lord & Son*

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4. The Eleventh Circuit expressly recognized in its opinion that the Florida Supreme Court's decision in *Federal Ins. Co. v. Southwest Fla. Retirement Ctr.*, 707 So. 2d 1119, 1121 (Fla.1998) thereafter declined to extend *Larkin General Hospital* beyond delay damages. (Petitioner's Appendix, p. 21).

> *Constr., Inc. v. Roberts Electrical Contractors, Inc.*, 624 So.2d 376, 377 n. 2 (Fla. 1st DCA 1993). Even after *Larkin General Hospital*, Florida courts have continued to utilize the well-established doctrine of incorporation by reference to impose liability on a performance bond surety. *See DCC Constructors, Inc. v. Randall Mech. Inc.*, 791 So.2d 575, 576-77 (Fla. 5th DCA 2001); *Southwest Fla. Retirement Ctr. v. Fed Ins. Co.*, 682 So.2d 1130, 1132-33 (Fla. 2d DCA 1996), *aff'd*, 707 So.2d 1119 (Fla.1998). The "purpose" of the performance bonds was to insure performance in accordance with the terms of the respective subcontracts, and those terms plainly include adverse direct consequences for delay. ***Therefore, under the particular facts of this case, the unequivocal delay damages provisions of the subcontracts are properly considered part of the bonds issued by National Fire because of the incorporation by reference.***

(Petitioner's Appendix, pp. 23-24). Based on the above stated reasoning, the Eleventh Circuit concluded that Fortune was entitled to the right to seek recovery of contractually mandated liquidated delay damages from National Fire. (Petitioner's Appendix, p. 24).

4. Petitioner's claimed conflict

Petitioner contends that the Eleventh Circuit's decision creates conflict with the Fifth Circuit's decision in *L & A Contracting Co. v. Southern Concrete Services*, 17 F.3d 106 (5th Cir. 1994). Specifically, Petitioner argues that the Eleventh Circuit interprets *Larkin* differently than did the

Fifth Circuit in *L & A Contracting*. *L & A Contracting*, however, did not involve a bond that incorporated by reference a subcontract with a specific provision for liquidated delay damages. In fact, the entire discussion in *L & A Contracting* of *Larkin* and of a surety's liability for delay damages was as follows:

> F & D [the surety] next challenges the district court's judgment holding it liable for delay damages. We need not linger long on this question because it is directly controlled by the Florida Supreme Court's opinion in *American Home Assurance Co. v. Larkin General Hospital, Ltd.* The *Larkin* Court held that "the surety's liability for damages is limited by the terms of the bond". The bond here contained no provision imposing liability on F & D for delay damages, and the district court may not imply such a provision. Therefore, the district court erred in holding F & D liable for delay damages.

17 F.3d at 112. The Eleventh Circuit's decision here does not conflict in any way with the *L & A Contracting* Court's few remarks on the extent of performance bond liability for delay damages. The Eleventh Circuit certainly did not 'imply' a delay damage provision where no such provision existed under the bonds' language. National Fire's own performance bonds each incorporated delay damage provisions by reference.

REASONS FOR DENYING THE PETITION

Petitioner contends that conflict between Circuits has been created as to an important matter and/or that the Eleventh Circuit has so far departed from the accepted and usual course of judicial proceedings as to call for exercise of this Court's supervisory powers. Respondent submits that neither circumstance is presented here, and that jurisdiction should accordingly be declined. Respondent also submits that misstatements of law and fact in Petitioner's brief present a further basis for denial of the request for a writ under Rule 14(4).

I. NO CONFLICT IS PRESENTED

The subject Eleventh Circuit decision, the Fifth Circuit's decision in *L & A Contracting,* and the Florida Supreme Court's decision in *Larkin* all stand for precisely the same propositions of law. All of the cases are in agreement that: (1) a surety bond is a contract and therefore subject to the general law of contracts; (2) a surety bond must accordingly be construed in accordance with its language and purpose; and (3) under these contract principles of construction, a surety bond will not be held to cover delay damages unless the contracting language of the bond specifically so provides.

As set out in the Eleventh Circuit's decision in this case, Petitioner's performance bonds here specifically incorporated the terms of the Arkin subcontracts by reference, and the subcontracts contained very specific liquidated delay damage provisions. The bonds here were accordingly held to cover the liquidated delay damage amounts.

The bonds in *L & A Contracting* and *Larkin* did *not* contain contracting language that incorporated by reference specific liquidated delay damage terms of the subcontracts, and the bonds in those cases were held not to cover delay damages for that reason. The Eleventh Circuit's decision here merely applies the law established in *Larkin* to a different set of facts then those presented in *L & A Contracting*. No conflict whatsoever has been created.

II. THE SUBJECT DECISION HAS NO NEW RAMIFICATIONS FOR THE SURETY INDUSTRY

Petitioner also advances the alarmist argument that the Eleventh Circuit's decision will place the entire surety industry in jeopardy by making it liable for delay damages never contemplated by the industry. This argument has neither factual nor legal support.

The Eleventh Circuit has merely reiterated the unexceptional principle that sureties will be obligated to the extent of the contract language in their bonds - neither more nor less. And, while sureties *may* use some of the standard forms developed by the industry, they are certainly not required to do so. Each surety is the master of its own fate in that regard, and thus has control over the extent of its obligations under its bonds. Petitioner National Fire here, for example, used standard form bonds for one of the projects, and drafted its own forms for the other. (Petitioner's Appendix, p. 2).

Furthermore, the fact that some performance bonds are held to cover actual and liquidated delay damages has long been known to the surety industry, not least from reported case law spanning many decades. *See, e.g., Continental*

Realty Corp. v. Andrew J. Crevolin Co., 380 F. Supp. 246 (S. D.W. Va. 1974) (surety that failed to perform under performance bond could be held liable for damages caused by delay, even where delay damage amounts exceeded the maximum penalty amount set by the bond); *Southern Roofing & Petroleum Co. v. Aetna Insurance Co.*, 293 F. Supp. 725 (E.D. Tenn. 1968) (surety was liable for ten percent liquidated delay damage penalty provided for in subcontract where bond specifically incorporated the subcontract's terms by reference); *New Amsterdam Casualty Company v. Mitchell*, 325 F.2d 474 (5th Cir. 1964) (surety on contractor's performance bond held liable for delay damages consisting of additional interest on construction loan occasioned by delay); *Miracle Mile Shopping Center v. National Union Indemnity Company*, 299 F.2d 780 (7th Cir. 1962) (surety held liable for delay damages caused by contractor's default and surety's failure to take over construction or pay for completion); *Mason* v. *City of Albertville*, 158 So. 2d 924 (Ala. 1963) (liquidated damages representing $100 per day for overrun of 381 days in completing sewer construction contract was a loss suffered under contract by obligee of contractor's performance bond, and such loss was covered by bond); *Industrial Indemnity Co. v. Wick Construction Co.*, 680 P.2d 1100 (Alaska 1984) (surety on performance bond held liable along with subcontractor for delay damages under liquidated delay damage provision in subcontract); *Cates Construction, Inc. v. Talbot*, 980 P.2d 407 (Cal. 1999) (bond and construction contract construed together to permit developer to recover delay damages from surety); *Pacific Employers Insurance Co. v. City of Berkeley*, 158 Cal. App. 3d 145 (Cal. 1st DCA 1984) (where performance bond incorporated construction contract by reference; surety was bound by contract's provision for liquidated delay damages); *Hemenway Company, Inc. v. Bartex, Inc. of Texas*,

373 So. 2d 1356 (La. 1st Cir. 1979) (surety held liable along with contractor for delay damages for untimely completion of project).

The surety industry has, in short, been aware that bonds may create potential liability for delay damages for more than sufficient time to react in whatever ways the industry deemed prudent, including in the drafting of the language of bonds and in assessing adequate premiums. Neither is there any novelty to the fact that the delay damage liability may be triggered by language in a bond incorporating by reference the terms of an underlying construction contract.

Petitioner has failed to demonstrate that the Eleventh Circuit departed in any way from the accepted and usual course of judicial proceedings with its decision. And, Respondent respectfully submits, Petitioner's suggestion that the Eleventh Circuit's decision "threatens to accidentally devastate the surety industry" (Petition, p. 14) is unsupported rhetoric that does not transform this case into one of exceptional importance calling for exercise of this Court's supervisory powers.

III. MISSTATEMENTS IN THE PETITION

The Petition asserts as a major theme throughout that the Eleventh Circuit did not understand the parties' claims as presented to the district court, and that accordingly the Eleventh Circuit did not have the benefit of briefs on the correct issues. For example, the Petition states at page 6: "As the Eleventh Circuit's opinion is largely devoted to its misunderstanding of the record, it did not have the benefit of briefs on issues that were not part of the record." (Petition, p. 6). The Eleventh Circuit's extremely thorough

opinion contradicts Petitioner's assertions in this regard. But, for present purposes, we note that it is inaccurate for Petitioner to state that the Eleventh Circuit was never given any briefing on these issues that the Petitioner claims the Eleventh Circuit misunderstood. In fact, Petitioner briefed all of the arguments for the Eleventh Circuit in its Amended Petition for Reconsideration, which we have included in an Appendix to this brief. (Respondent's Appendix, pp. 1a-11a).

The Amended Petition for Rehearing shows that Petitioner presented the Eleventh Circuit with briefing on *all* of the issues that the Petition states were never briefed for the Eleventh Circuit. In fact, the arguments in the Amended Petition for Rehearing are repeated almost verbatim in the Petition filed with this Court. It is thus not true that the Eleventh Circuit did not have the benefit of briefing on the issues presented herein.

The Petitioner goes on to state that "the Eleventh Circuit also apparently did not consider the more recent Florida Supreme Court case of *Federal Insurance Co. v. Southwest Florida Retirement Center, Inc.*, 707 So. 2d 1119 (Fla. 1998)." (Petition, p. 12). In fact, the Eleventh Circuit's decision ***expressly*** acknowledges that case, and accurately notes its holding refusing to extend *Larkin* beyond delay damages. (Petitioner's Appendix, p. 21).

The Petition also states:

> Under the holding of these cases [referring to *Larkin* and *L & A Contracting*], if a performance bond specifies that it incorporates the underlying contract, but it does not specify on its face that the surety is responsible for delay damages arising

> from untimely performance of the underlying contract, liability for delay damages is not imposed on the surety.

(Petition, p. 6). This is clearly a misstatement of the holdings of these cases. As discussed in full above, the cases hold that the coverage of a performance bond will be determined under ordinary contract construction principles. Neither the *Larkin* nor *L & A Contracting* bonds incorporated by reference subcontracts with specific provisions for payment of delay damages, so, under ordinary contract law principles, the *Larkin* and *L & A Contracting* sureties were held to have no liability for delay damages. Neither decision says that liability for delay damage will not be imposed on a surety whose bond incorporates a delay damage provision by reference rather than stating it on the face of the bond.

Finally, the Petition makes the following direct misstatements of fact:

> Next, the Eleventh Circuit ***mistakenly believed that Fortune sought to recover the liquidated delay damages from National Fire in the underlying suit under a theory that they were the responsibility of National Fire under the performance bonds. Such a theory was not pled or otherwise asserted by Fortune before the District Court,*** likely because it was expressly barred by the Florida Supreme Court's holding in Larkin[.] . . . ***To attempt to avoid the holding of Larkin General Hospital , Fortune framed its theory of delay damages as a "set-off" that could***

> ***be applied to Arkin's unpaid contract balances, rather than an affirmative claim for recovery of damages under the performance bond.***

(Petition, pp. 5-6). The fact is that Fortune filed not only an answer and affirmative defenses claiming set-offs, but also a counterclaim which, in Count I, claimed ***precisely*** those damages from National Fire and on ***precisely*** that theory. A copy of Fortune's Answer and Counterclaim have accordingly been included in the Respondent's Appendix hereto. (Respondent's Appendix, pp. 12a-22a). Count I reads, in pertinent portion:

COUNTERCLAIM

* * *

COUNT I

* * *

9. In addition, FORTUNE demanded that NATIONAL FIRE honor its obligations under the Performance Bond attached hereto as Exhibit "B".

10. Despite said demands, NATIONAL FIRE has failed and refused to honor its obligations under the aforesaid surety bond and has breached not only its obligation to remedy the default of its principal, ARKIN, but also its obligation to perform those duties set forth in the bond as surety.

11. By virtue of the aforesaid default by ARKIN, ***as well as the breach of the obligations under***

> ***the Performance Bond by NATIONAL FIRE, Counterclaimant has been damaged.***
>
> 12. ***The damages incurred by Counterclaimant*** are in excess of $15,000 and ***include, but are not limited to, the following which may encompass consequential and/or special damages contemplated by the parties:***
>
> * * *
>
> (e) Impact to other projects, including interest and ***delay expenses;***
>
> * * *
>
> (h) ***Delay damages*** caused by the failure of the surety to perform its obligations[.]

(Respondent's Appendix, pp. 16a-18a).

Further, the Eleventh Circuit's decision confirms that the Eleventh Circuit was well-acquainted with the actual record, and with the fact that Respondent Fortune had raised *both* set-off claims *and* affirmative claims for damages under the performance bond as to the delay damages:

> Fortune contends that National Fire is responsible for liquidated delay damages that had accrued prior to Arkin's default due to Arkin's failure to timely perform on both projects. Although Fortune obtained judgment as a matter of law against Arkin

> for these damages, ***Fortune seeks to set these damages off against the retained contract balances. Fortune also argues that National Fire is contractually liable for these damages because the bonds incorporated by reference the underlying subcontracts which expressly provided for delay damages.***

(Petitioner's Appendix, p. 20).

The foregoing misstatements of law and fact are such that Petitioner has failed to make an accurate presentation as required by Rule 14(4), justifying denial of the Petition on that basis alone.

CONCLUSION

Based on the foregoing facts and authorities, Respondent respectfully submits that the Petitioner's request for a writ of certiorari should be denied.

Respectfully submitted,

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APPENDIX

APPENDIX A — AMENDED PETITION FOR RECONSIDERATION OF NATIONAL FIRE INS. CO. OF HARTFORD DATED MARCH 6, 2003 FILED IN THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

Docket No. 01-15124F

Case No. 97-2439-Civ-King

FORTUNE CONSTRUCTION CO., INC.,

Appellant,

v.

NATIONAL FIRE INSURANCE COMPANY OF HARTFORD,

Appellee,

On Appeal from United States District Court
for the Southern District of Florida

NATIONAL FIRE INSURANCE COMPANY OF HARTFORD'S AMENDED PETITION FOR RECONSIDERATION

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Appendix A

UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

Docket No. 01-15124F

Case No. 97-2439-Civ-King

FORTUNE CONSTRUCTION CO., INC.,

Appellant,

v.

NATIONAL FIRE INSURANCE COMPANY
OF HARTFORD,

Appellee,

On Appeal from United States District Court
for the Southern District of Florida

NATIONAL FIRE INSURANCE COMPANY OF HARTFORD'S AMENDED PETITION FOR RECONSIDERATION

Plaintiff/Appellee, National Fire Insurance Company of Hartford ("National Fire") respectfully petitions for Reconsideration of the Opinion filed February 7, 2003 (the "Opinion"). The grounds for this petition include:

(1) The Parties apparently failed to adequately explain the record of this convoluted case, as the Opinion is largely directed to the issue that "[t]he district court erred to the extent that it granted summary judgment for National Fire

on its claim of equitable subrogation arising out of the performance bonds." The district court did not grant summary judgment for National Fire on a claim of equitable subrogation arising out of the performance bonds. National Fire did not even make such a claim in this case, or bring such a motion, and this issue was not a subject of the appeal.

(2) Perhaps as a result of the Court addressing an issue not contemplated by the parties, and therefore not adequately addressed in the briefs, the Opinion makes an obvious fact error in the manner that it distinguishes the Florida Supreme Court case of *American Home Assurance Co. v. Larkin General Hospital, Ltd.*, 593 So. 2d 195 (Fla. 1992). Specifically, the Opinion turns upon the suggested distinction that the bond in *Larkin General Hospital* did not incorporate the underlying construction contract. However, reported Florida decisions that do set forth the specific terms of the performance bond under consideration in *Larkin General Hospital* show the performance bond to be identical in this regard to the performance bond in the instant case. The Opinion thus turns on this fact error.

(3) Once this incorrect distinction is removed, it is apparent that the "incorporation analysis" applied by the Opinion to expand the liability of a performance bond surety is inconsistent with *Larkin General Hospital* and its progeny, *Federal Insurance Co. v. Southwest Florida Retirement Center, Inc.*, 707 So. 2d 1119 (Fla. 1998).

(4) The Opinion did not have the benefit of considering a very recent case on-point that was decided and published

after the submission of briefs. This recent authority directly contradicts the Opinion in its interpretation of *Larkin General Hospital* and *Southwest Florida Retirement*.

I. The Holding and Analysis of the Opinion is Misplaced as it Addresses Whether National Fire is Entitled to Equitable Subrogation Arising Out of the Performance Bonds. This was Not an Issue in the Case.

A lengthy portion of the Opinion is devoted to an analysis of whether National Fire was entitled to equitable subrogation rights arising out of the performance bonds. A holding of the Opinion is that "[t]he district court erred to the extent that it granted summary judgment for National Fire on its claim of equitable subrogation arising out of the performance bonds." However, this holding and analysis is misplaced and arises from an apparent misinterpretation of the record. The district court never granted summary judgment for National Fire on a claim of equitable subrogation arising out of the performance bonds. National Fire never moved for summary judgment on a claim of equitable subrogation arising out of the performance bonds. National Fire did not assert such a claim in this case, and indeed, would have no basis for such a claim in this context as it did not expend any funds to complete the work.

The misinterpretation of the record may have arisen because the Order granting National Fire's Motion for Partial Summary Judgment is not a model of clarity. However, the Motion itself, entitled "National Fire's First Motion for

Partial Summary Judgment (Payment Bond Equitable Subrogation)" is clear. Paragraph 4 states as follows:

> This motion is based upon, and limited to, the rights and obligations arising from the two payment bonds. It is not intended to touch upon issues related to the two performance bonds. This motion is solely intended to resolve legal disputes regarding rights and obligations under the payment bonds.

As the question of whether National Fire was entitled to equitable subrogation rights arising out of the performance bonds was not an issue in this case, it should not be a focus of the Opinion. Certainly, the Opinion should not hold that "[t]he district court erred to the extent that it granted summary judgment for National Fire on its claim of equitable subrogation arising out of the performance bonds" when no such grant of summary judgment occurred, and no such claim was asserted.

II. The Opinion Distinguishes *Larkin General Hospital* Based Upon the Incorrect Belief that the Performance Bond in that Case Did Not Incorporate the Contract.

The unnecessary consideration in the Opinion of the issue of whether National Fire had any equitable subrogation rights under the performance bond unfortunately led to an incorrect interpretation of *American Home Assurance Co. v. Larkin General Hospital, Ltd.*, 593 So. 2d 195 (Fla. 1992). The Court did not have the benefit of a thorough briefing on this issue and perhaps as a result mistakenly distinguished *Larkin*

General Hospital in the Opinion as follows: "[h]owever, unlike the performance bond in *Larkin General Hospital*, the bonds at issue in this case expressly incorporated the subcontracts." This is just factually wrong, although it requires a review of a reported decision that was not brought to the attention of the Court to appreciate that the performance bond under consideration in *Larkin General Hospital* also expressly incorporated the underlying construction contract. Indeed, the terms of the performance bond in *Larkin General Hospital* not only incorporated the contract, but are almost exactly the same as the terms of the performance bonds in the instant case.

The opinion in *Larkin General Hospital* did not expressly set forth the terms of the performance bond. However, the Court did state that "[t]he language of the performance bond in the case at bar is identical to the language in the performance bond in *Arbor Club, Inc. v. Omega Constr. Co.*, 565 So. 2d 357 (Fla. 4th DCA 1990)." *Larkin General Hospital*, 593 So. 2d at 197. The Fourth District opinion in *Arbor Club* did set forth terms of that performance bond, specifically stating that "[t]he bond also provides that the contract between Omega and Arbor 'is by reference made a part hereof.'" *Arbor Club*, 565 So. 2d at 359. Thus, it is apparent that the performance bond in *Larkin General Hospital*, having language that is identical to the performance bond in *Arbor Club* that incorporated the contract, also incorporated the contract. Thus, the basis for distinguishing *Larkin General Hospital* in the Opinion is incorrect.

III. Once the Incorrect Distinction of *Larkin General Hospital* is Removed, it is Apparent that the Florida Supreme Court Rejected the Incorporation Analysis Applied by the Instant Opinion.

Larkin General Hospital reached the Florida Supreme Court based upon a certification of conflict between *Arbor Club of Boca Raton, Inc. v. Omega Constr. Co.*, 565 So. 2d 357 (Fla. 4th DCA 1990) and *United States Fidelity & Guar. Co. v. Gulf Florida Dev. Corp.*, 365 So. 2d 748 (Fla. 1st DCA 1978). As discussed above, the consideration in the Opinion of whether National Fire had any equitable subrogation rights under the performance bond unfortunately led to an incorrect means of distinguishing *Larkin General Hospital.* To compound that error, the Opinion uses the same analysis and reaches the same conclusion as in *Arbor Club.* This interpretation and holding was expressly rejected in *Larkin General Hospital.* In other words, without the benefit of briefs on this issue, and due to the mistaken distinction that the bond in *Larkin General Hospital* did not incorporate the contract, the Opinion erroneously reached the same interpretation and holding that was previously rejected by the Florida Supreme Court. Moreover, in a case that was apparently not considered by the Opinion on this point, the Florida Supreme Court recently expressly reaffirmed that *Larkin General Hospital* should be interpreted as rejecting the incorporation analysis adopted by the Opinion. *Federal Insurance Co. v. Southwest Florida Retirement Center, Inc.*, 707 So. 2d 1119 (Fla. 1998).

Arbor Club, Gulf Florida, Larkin General Hospital and the instant case all involved performance bonds that

incorporated the underlying contracts, but did not specify on their face that the surety was responsible for delay damages. The basis of the holding in *Arbor Club* was that "the bond incorporated the construction contract by reference, and that contract provided for timely performance." *Arbor Club*, 565 So. 2d at 360. Thus, the *Arbor Club* court held the performance bond surety liable for delay damages. In conflict with *Arbor Club*, the First District in *Gulf Florida*, faced with the same language in another performance bond, concluded that the terms of the performance bond limited the liability of the surety to the costs of completion and the costs of curing defective work. *Larkin General Hospital*, 593 So. 2d at 197. The Florida Supreme Court expressly adopted the holding of *Gulf Florida* and rejected the incorporation analysis of *Arbor Club*:

> The court in *Arbor Club* failed to construe the language in the performance bond in harmony with the subject matter of the bond and with the purpose of the bond. The purpose of a performance bond is to guarantee the completion of the contract upon default by the contractor. Ordinarily a performance bond only ensures the completion of the contract. The surety agrees to complete the construction or to pay the obligee the reasonable costs of completion if the contractor defaults.
>
> The liability of a surety is coextensive with that of the principal. However, the surety's liability for damages is limited by the terms of the bond. Florida courts have long recognized that the

> liability of a surety should not be extended by implication beyond the terms of the contract; i.e., the performance bond.
>
> We agree with the holding in *Gulf Florida* and with the court's interpretation of the performance bond language. Accordingly, we reject the holding and interpretation of the performance bond language in *Arbor Club* and *Wolley/Sweeney*. The terms of the performance bond control the liability of American [the surety]. The language in the performance bond, construed together with the purpose of the bond, clearly explains that the performance bond merely guaranteed the completion of the construction contract and nothing more. Upon default, the terms of the performance bond required American to step in and either complete construction or pay Larkin the reasonable costs of completion. Because the terms of the performance bond control the liability of the surety, American's liability will not be extended beyond the terms of the performance bond. Therefore, American cannot be held liable for delay damages.

Larkin General Hospital, 593 So. 2d at 198 (internal cites omitted). When the above holding is read with the understanding that the performance bonds in *Larkin General Hospital*, *Arbor Club*, *Gulf Florida*, and the instant case all incorporated the underlying construction contracts, it is apparent that the instant Opinion has misinterpreted *Larkin General Hospital*.

IV. The Florida Supreme Court Recently Confirmed that *Larkin General Hospital* Should be Interpreted to Reject the Incorporation Analysis. Additional Recent Case-Law, Published After the Submission of Briefs, Concurs in Interpreting *Larkin General Hospital* and Florida Law to Reject the Incorporation Analysis.

The Florida Supreme Court recently expressly reaffirmed that the proper interpretation of *Larkin General Hospital* is that the liability of a performance bond surety may not be extended by "contractual incorporation." *Federal Insurance Co. v. Southwest Florida Retirement Center, Inc.*, 707 So. 2d 1119 (Fla. 1998). Specifically, the Court adopted the reasoning of the lower court's dissent and held that the "incorporation" analysis improperly "extends the liability on the bond by implication beyond the terms of the bond contract. This additional burden is in derogation of the analysis provided by *Larkin General Hospital*." *Id.* at 1120-1121. Thus, following *Southwest Florida*, it is beyond doubt that the Florida Supreme Court does not agree with the "incorporation" analysis relied upon in the instant Opinion.

The most recent reported decision to interpret *Larkin General Hospital* is *Auto Owners Insurance Company v. Travelers Casualty & Surety Co.*, 227 F.Supp.2d 1248 (M.D. Fla. 2002). As this decision is dated September 12, 2002, after the submission of briefs in this case, it presumably was not considered by the Court. The Middle District undertook an extensive evaluation and discussion of both *Larkin General Hospital* and the subsequent Supreme Court opinion in *Southwest Florida Retirement*. *Auto Owners*, 227 F.Supp.2d at 1264-1265. The *Auto Owners* opinion explains

that in *Southwest Florida Retirement*, the Florida Supreme Court expressly "rejected the owner's argument that a surety's liability is co-extensive with the general contractor based on incorporation of the general contract into the performance bond." *Id.* at 1265. Similarly, the *Auto Owners* court found that "[a] holding that the incorporation provision may enlarge a surety's obligation under a bond, for both costs to complete a project and for damages that result from the project, would seem contrary to *Larkin*." *Id. Auto Owners* is simply one more example of established Florida law — a surety's liability is not extended by incorporation of the subcontract into the bond. The Opinion is contrary to that established principle.

CONCLUSION

The irony of this request for reconsideration is that granting it and correcting the obvious factual error in the Opinion regarding the interpretation of *Larkin General Hospital* will not vary the monetary result. However, the Opinion's favorable consideration of the incorporation argument rejected by the Florida Supreme Court in *Larkin General Hospital* can only serve to confuse an aspect of the law of suretyship in Florida which is now clear. Since *Larkin General Hospital*, owners, sureties and contractors have understood the rights and responsibilities they were undertaking in relation to consequential damages on bonded projects. That understanding leads to the clarity required to make intelligent business decisions. The Opinion will undermine that ability.

National Fire respectfully requests that the Court revisit the opinion and grant reconsideration on the points raised above.

* * * *

APPENDIX B — ANSWER AND AFFIRMATIVE DEFENSES OF FORTUNE CONSTRUCTION CO. DATED AUGUST 20, 1997 FILED IN THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF FLORIDA

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA

CASE NO: 97-2439 CIV-KING

NATIONAL FIRE INSURANCE COMPANY OF HARTFORD, a Connecticut corporation,

Plaintiff,

vs.

FORTUNE CONSTRUCTION COMPANY, a Florida corporation,

Defendant.

ANSWER AND AFFIRMATIVE DEFENSES

Defendant, FORTUNE CONSTRUCTION COMPANY (hereinafter "FORTUNE"), files this Answer to the Complaint of Plaintiff, NATIONAL FIRE INSURANCE COMPANY OF HARTFORD (hereinafter "NATIONAL FIRE"), and says:

1. As and for its answer to Paragraph 1, the same is admitted.

2. As and for its answer to Paragraph 2, the same is admitted.

Appendix B

3. As and for its answer to Paragraph 3, FORTUNE is without knowledge of the same and, therefore, denies the same and demands strict proof thereof.

COUNT I

4. As and for its answer to Paragraph 4, FORTUNE is without knowledge of the allegations contained therein and, therefore, denies the same and demands strict proof thereof.

5. As and for its answer to Paragraph 5, FORTUNE admits that NATIONAL FIRE issued bonds wherein FORTUNE was the obligee. In addition, FORTUNE admits it was the general contractor upon the projects known as West Brickell Apartments and Tract "G" at Winston Park, Coconut Creek, Florida. However, the bonds attached are not true copies of the originals of the same and, therefore, the remaining allegations of Paragraph 5 are denied.

6. FORTUNE admits that Arkin Construction Company, Inc. defaulted on the projects for which the bonds were issued by NATIONAL FIRE, but denies the remaining allegations contained in Paragraph 6.

7. As and for its answer to Paragraphs 7 and 8, the same are denied.

COUNT II

8. As and for its answer to Paragraph 9, FORTUNE realleges and reavers its previous responses to Paragraphs 1 through 3.

9. As and for its answer to Paragraph 10, FORTUNE is without knowledge of the allegations contained therein and, therefore, denies the same and demands strict proof thereof.

10. As and for its answer to Paragraph 11, the same is denied.

AFFIRMATIVE DEFENSES

That as and for its further Answer and Affirmative Defenses, Defendant, FORTUNE, says:

1. All allegations not specifically admitted herein are denied.

2. As reflected in the Complaint filed herein, Arkin Construction Company, Inc., the principal upon the bond, defaulted under the terms of its subcontract agreement. By virtue of said default and otherwise, FORTUNE has incurred damages and other expenses, including cost of completion, to the extent that there are no contract sums due to Arkin Construction Company, Inc. and, in fact, damages are due from Arkin Construction Company, Inc. to FORTUNE.

3. Upon the default of Arkin Construction Company, Inc. as set forth in the Complaint, demand was made upon Plaintiff, NATIONAL FIRE, to honor its bond obligations with regard to the Payment and Performance Bonds executed and delivered to FORTUNE with regard to the subject projects. NATIONAL FIRE failed and/or refused to so honor said obligations, thereby breaching the terms of its bonds.

NATIONAL FIRE is responsible to FORTUNE for damages incurred by FORTUNE arising from the default of Arkin Construction Company, Inc. and the default of NATIONAL FIRE, which damages are in excess of any contract balances at issue herein.

4. FORTUNE incorporates herein the allegations of its Counterclaim hereinafter set forth and further says that by virtue of the actions set forth therein, NATIONAL FIRE should be barred or is estopped to assert any claims against FORTUNE.

5. The actions of Plaintiff, NATIONAL FIRE, upon notice of default and demand for performance were such as to constitute bad faith and, as a result of the same, NATIONAL FIRE should be barred or estopped from any claim in this matter.

6. The actions of Plaintiff, NATIONAL FIRE, with regard to the projects in question constitute actions taken with unclean hands, thereby barring or estopping any claims herein.

7. As a result of the actions of NATIONAL FIRE, FORTUNE has been required to employ the undersigned attorneys to represent them in this matter and is entitled to attorney's fees in the defense of this action.

WHEREFORE, having fully answered the Complaint of Plaintiff, NATIONAL FIRE INSURANCE COMPANY OF HARTFORD, Defendant, FORTUNE CONSTRUCTION COMPANY, prays that the Court enter Judgment in its favor

and against Plaintiff and grant to Defendant, FORTUNE CONSTRUCTION COMPANY, all costs, expenses, and reasonable attorney's fees incurred in the defense hereof.

COUNTERCLAIM

Counterclaimant, FORTUNE CONSTRUCTION, INC. (hereinafter "FORTUNE"), files this Counterclaim against Counterdefendant, NATIONAL FIRE INSURANCE COMPANY OF HARTFORD (hereinafter "NATIONAL FIRE"), and joins as an additional Counterdefendant, ARKIN CONSTRUCTION COMPANY, INC. (hereinafter "ARKIN"), and says:

1. This is an action for damages in excess of $15,000.

2. Counterclaimant, FORTUNE, is a Florida corporation with its principal office located in Dade County, Florida.

3. Counterdefendant, ARKIN, is a Florida corporation with its principal office located in Dade County, Florida.

4. Counterdefendant, NATIONAL FIRE is a Connecticut corporation authorized to issue surety bonds in the State of Florida.

COUNT I

5. On or about February 21, 1996, Counterclaimant, FORTUNE, and Counterdefendant, ARKIN, entered into a contract for the construction of a project described as Tract "G" at Winston Park, Coconut Creek, Florida. A true copy of said contract is attached hereto as Exhibit "A".

6. In connection with and conditioned to the performance of said contract, Counterdefendants, NATIONAL FIRE, as surety, and ARKIN, as principal, did execute and deliver to Counterclaimant a Performance Bond wherein FORTUNE was the named obligee. A true copy of the Performance Bond, including a Dual Obligee Rider, is attached hereto as Composite Exhibit "B".

7. ARKIN commenced construction of the project and continued with the same until abandoning the project on or about May 29, 1997.

8. Thereafter, Counterclaimant, FORTUNE, declared ARKIN in default of its contract obligations and notified NATIONAL FIRE of the same.

9. In addition, FORTUNE demanded that NATIONAL FIRE honor its obligations under the Performance Bond attached hereto as Exhibit "B".

10. Despite said demands, NATIONAL FIRE has failed and refused to honor its obligations under the aforesaid surety bond and has breached not only its obligation to remedy the default of its principal, ARKIN, but also its obligation to perform those duties set forth in the bond as surety.

11. By virtue of the aforesaid default by ARKIN, as well as the breach of the obligations under the Performance Bond by NATIONAL FIRE, Counterclaimant has been damaged.

12. The damages incurred by Counterclaimant are in excess of $15,000 and include, but are not limited to, the

following which may encompass consequential and/or special damages contemplated by the parties:

(a) Direct and indirect project completion costs;

(b) Payments to subcontractors, laborers, and materialmen;

(c) Increased overhead and administrative expenses;

(d) Interest expenses;

(e) Impact to other projects, including interest and delay expenses;

(f) Lost opportunity to undertake other projects;

(g) Lost profits;

(h) Delay damages caused by the failure of the surety to perform its obligations; and

(i) Contractual damages due from FORTUNE to owner.

13. All conditions precedent to this action have been performed, have occurred, or have been waived.

14. As a result of the actions of Counterdefendant, NATIONAL FIRE, Counterclaimant has been required to

employ the services of the undersigned counsel to represent it in this matter and has agreed to pay a reasonable fee for their services.

WHEREFORE, Counterclaimant, FORTUNE CONSTRUCTION, INC., prays that the Court enter Judgment against Counterdefendants, NATIONAL FIRE INSURANCE COMPANY OF HARTFORD and ARKIN CONSTRUCTION COMPANY, INC., for all damages incurred, including those consequential and special damages listed above, together with interest, costs, and reasonable attorney's fees.

COUNT II

15. Counterclaimant realleges and reavers Paragraphs 1 through 4 as if more fully set forth herein.

16. On or about January 15, 1996, FORTUNE and Counterdefendant, ARKIN, entered into a contract for the construction of a project known as West Brickell — 130 Apartments — Miami, Florida. A true copy of said contract is attached hereto as Exhibit "C".

17. In connection with and conditioned to the performance of said contract, Counterdefendants, NATIONAL FIRE, as surety, and ARKIN, as principal, did execute and deliver to Counterclaimant a Performance Bond wherein FORTUNE was the named obligee. A true copy of the Performance Bond is attached hereto as Exhibit "D".

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18. ARKIN commenced construction of the project and continued with the same until abandoning the project on or about May 29, 1997.

19. Thereafter, Counterclaimant, FORTUNE, declared ARKIN in default of its contract obligations and notified NATIONAL FIRE of the same.

20. In addition, FORTUNE demanded that NATIONAL FIRE honor its obligations under the Performance Bond attached hereto as Exhibit "D".

21. Despite said demands, NATIONAL FIRE has failed and refused to honor its obligations under the aforesaid surety bond and has breached not only its obligation to remedy the default of its principal, ARKIN, but also its obligation to perform those duties set forth in the bond as surety.

22. By virtue of the aforesaid default by ARKIN, as well as the breach of the obligations under the Performance Bond by NATIONAL FIRE, Counterclaimant has been damaged.

23. The damages incurred by Counterclaimant are in excess of $15,000 and include, but are not limited to, the following which may encompass consequential and/or special damages contemplated by the parties:

(a) Direct and indirect project completion costs;

(b) Payments to subcontractors, laborers, and materialmen;

Appendix B

(c) Increased overhead and administrative expenses;

(d) Interest expenses;

(e) Impact to other projects, including interest and delay expenses;

(f) Lost opportunity to undertake other projects;

(g) Lost profits;

(h) Damages caused by the failure of the surety to timely and properly perform its obligations;

(i) Rental loss;

(j) Additional marketing expenses;

(k) Finance penalties;

(l) Loss of reputation; and

(m) Contractual damages due from FORTUNE to owner.

24. All conditions precedent to this action have been performed, have occurred, or have been waived.

25. As a result of the actions of Counterdefendant, NATIONAL FIRE, Counterclaimant has been required to

employ the services of the undersigned counsel to represent it in this matter and has agreed to pay a reasonable fee for their services.

WHEREFORE, Counterclaimant, FORTUNE CONSTRUCTION, INC., prays that the Court enter Judgment against Counterdefendants, ARKIN CONSTRUCTION COMPANY, INC. and NATIONAL FIRE INSURANCE COMPANY OF HARTFORD, for all damages incurred, including those consequential and special damages listed above, together with interest, costs, and reasonable attorney's fees.

* * * *